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Supreme Court of the United States

October Term, 1944

No. 515

FERDINAND W. ROEBLING, III,
Petitioner,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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Supreme Court of the United States

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No.....

FERDINAND W. ROEBLING, III,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

The petitioner, Ferdinand W. Roebling, III, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Third Circuit in the above case affirming a decision of The Tax Court of the United States.

Opinions Below

The memorandum opinion of The Tax Court (R. 15-25) is unreported. The opinion of the Circuit Court of Appeals .....F. (2d) .....appears at pages 38-46 of the Record.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered on July 1, 1944 (R. 46). The jurisdiction of this

Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. (U. S. C., Title 28, Section 347(a); see also U. S. C., Title 26, Section 1141(a).)

Questions Presented

1. Should the recognition of gain from the exchange of certain stock for 100-year non-callable bonds pursuant to a statutory merger be deferred under section 112(b)(3) of the Revenue Act of 1938?

(a) Does a merger of one corporation into another in accordance with the corporation laws of New Jersey constitute a reorganization under section 112(g)(1)(A) of the Revenue Act of 1938?

(i) Does the continuity of interest test as applied in *LeTulle* v. *Scofield*, 308 U. S. 415, have any application in the case of a true merger consummated in accordance with state law after the amendments to the reorganization provisions contained in the Revenue Act of 1934 and subsequent acts?

(ii) In any event, under the peculiar facts in this case, is the requisite continuity of interest present?

Statutes, Regulations & Committee Reports

New Jersey Statutes

The pertinent provisions of The General Corporation Law of New Jersey appear at pages 26-28 of the Record.

Federal Statutes

Revenue Act of 1938, c. 289, 52 Stat. 447:

"Sec. 112. Recognition of Gain or Loss.

"(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

"(b) *Exchanges Solely in Kind.*—

" * * * * * *

" * * * * * *

"(3) Stock for stock on reorganization.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan or reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

* * * * * * *

"(g) *Definition of Reorganization.*—As used in this section and section 113—

"(1) The term 'reorganization' means (A) a statutory merger or consolidation, or (B) the acquisition by one corporation in exchange solely for all or a part of its voting stock: of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation, or (C) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred, or (D) a recapitalization, or (E) a mere change in identity, form, or place of organization, however effected.

"(2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of a reorganization resulting from the acquisition by one corporation of stock or properties of another."

REGULATIONS

Treasury Regulations 101, promulgated under the Revenue Act of 1938:

"Art. 112(g)-2. *Definition of terms.*—The application of the term 'reorganization' is to be strictly limited to the specific transaction set forth in section 112(g)(1). The term does not embrace the mere purchase by one corporation of the properties of another corporation, for it imports a continuity of interest on the part of the transferor or its stockholders in the properties transferred. If the properties are transferred for cash and deferred payment obligations of the transferee evidenced by short-term notes, the transaction is a sale and not an exchange.

"The words 'statutory merger or consolidation' refer to a merger or a consolidation effected in pursuance of the corporation laws of the United States or a State or Territory or the District of Columbia.

* * * * * * *

"The term 'a party to a reorganization' includes, in addition to a corporation which performs the specific act constituting the reorganization as described and defined in section 112(g)(1), only a corporation specified in section 112(g)(2). Both corporations are parties to the reorganization if under statutory authority Corporation A is merged into Corporation B;

* * * * * * *

"Art. 112(g)-3. *Exchanges solely of stock or securities, or property, solely for stock or securities, in pursuance of plan of reorganization.*—No taxable income is received, nor is a deductible loss sustained, if the shareholders in a corporation a party to the following reorganization transactions exchange stock or securities solely for stock or securities of the same corporation, or of another corporation mentioned, or if one of such corporations transfers property to another of the corporations solely for stock or securities of such other corporation, in pursuance of the plan of reorganization:

"(1) The merger of Corporation A, in accordance with statutory authority, into Corporation B;"

COMMITTEE REPORTS

The parts of the reports of the Committee on Ways & Means and of the Committee on Finance dealing with "Exchanges & Reorganizations" under the Revenue Bill of 1934 are reproduced in full at pages 31-36 of the Record.

Statement

This proceeding originated in The Tax Court of the United States, which entered an order redetermining petitioner's income taxes for 1938 (R. 25). The issue is one of law. The facts as stipulated are fairly summarized in the Memorandum Opinion of The Tax Court (R. 15-25).

(1) In 1938 petitioner owned 166 shares of stock in South Jersey Gas, Electric & Traction Company (hereinafter called South Jersey) which had a tax basis in his hands of par, or $16,600 (R. 16).

(2) Since 1903 all the properties of South Jersey had been under lease for a 900-year term. The lease, after relieving South Jersey of all carrying charges, provided for a cash rental exactly sufficient to permit the payment to the stockholders of South Jersey of a dividend of 8% per annum on the par value of its capital stock and a cash dividend at that rate was regularly paid (R. 16-17).

(3) In November 1938, in order to eliminate this highly objectionable lease on the best possible terms,[1] South Jersey, the lessor, was merged into Public Service Electric & Gas Company, the lessee, in strict accordance with the corporation laws of New Jersey. This was accomplished under a plan of reorganization and a formal Agreement of Merger by the exchange of South Jersey stock, par for par, for 100-year non-callable 8% bonds of Public Service Electric & Gas Company, the continuing company. This plan was adopted in order to meet the tests prescribed

[1]See, Findings and Opinion of Federal Power Commission (R. 3-15).

by the New Jersey courts in *Outwater* v. *Public Service Corporation*, 103 N. J. Eq. 461, 143 Atl. 729, *aff'd*, 146 Atl. 916 (R. 17-21). Both The Tax Court (R. 23) and the Circuit Court of Appeals (R. 42) accepted the transaction as a true statutory merger under New Jersey law.

(4) In the transaction, the petitioner received in exchange for his 166 shares of South Jersey stock, having a tax basis of par, $16,600 principal amount of 100-year non-callable 8% bonds of Public Service Electric & Gas Company which had a fair market value of $34,777 (R. 21).

(5) The Commissioner of Internal Revenue determined that the difference between the basis of petitioner's stock in South Jersey and the fair market value of the bonds received in exchange therefor must be recognized as taxable income in 1938. The Tax Court and the Circuit Court of Appeals sustained that determination.

(6) The petitioner contends that the merger of South Jersey into Public Service Electric & Gas Company pursuant to the laws of the State of New Jersey, being a statutory merger, constituted a reorganization under section 112(g)(1)(A) of the Revenue Act of 1938, and that under section 112(b)(3) of that Act, the gain from the exchange by the petitioner, pursuant to such reorganization, of his stock in South Jersey for securities of the continuing company is not presently recognized. More specifically, he contends that the continuity of interest test, as applied in *LeTulle* v. *Scofield*, 308 U. S. 415, has no application in the case of a true merger consummated in accordance with State law after the amendments to the reorganization provisions contained in the Revenue Act of 1934 and subsequent Acts. In any event, he contends that, under the peculiar facts in this case, the requisite continuity of interest is present.

Specification Of Errors To Be Urged

The Circuit Court of Appeals erred:

(1) In holding that the recognition of petitioner's gain from the exchange of his South Jersey stock for 100-year non-callable 8% bonds of Public Service Electric & Gas Company pursuant to a statutory merger should not be deferred under section 112(b)(3) of the Revenue Act of 1938.

(2) In holding that a "true statutory merger" under New Jersey law is not a "statutory merger" within the meaning of section 112(g)(1)(A) of the Revenue Act of 1938.

(3) In holding that the continuity of interest test, as applied in *LeTulle* v. *Scofield*, 308 U. S. 415, is applicable in the case of a true merger consummated in accordance with state law after the amendments to the reorganization provisions contained in the Revenue Act of 1934 and subsequent Acts.

(4) In failing to hold that in any event under the peculiar facts in this case the requisite continuity of interest was present.

Reasons For Granting The Writ

The Circuit Court of Appeals in holding that the continuity of interest doctrine developed by this Court under the loosely worded definition of the term, reorganization, contained in the Revenue Acts of 1924, 1926, 1928 and 1932 should be applied to the precisely worded amended definition contained in the Revenue Act of 1934 and subsequent Acts, has decided an important question of Federal tax law which has not been, but should be, settled by this Court.

Section 112(i)(1) of the Revenue Act of 1932 and corresponding sections of the three earlier Acts provided that the term, reorganization, means, among other things:

> "(A) *a merger or consolidation (including the acquisition by one corporation of* at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or *substantially all the properties of another corporation),* * * * " [Italics ours]

This definition failed to spell out with precision the types of transactions contemplated as reorganizations by the parenthetical clause. A literal interpretation would have embraced sales for cash or short-term purchase money notes. In order to avoid that result, the continuity of interest test was developed as a gloss upon the generality of the language contained in the parenthetical clause. *Cortland Specialty Company* v. *Commissioner* (1932), 60 F. (2d) 937 (C. C. A. 2d); *Pinellas Ice & Cold Storage Company* v. *Commissioner* (1933), 287 U. S. 462; *Helvering* v. *Minnesota Tea Co.* (1935), 296 U. S. 378; *John A. Nelson Co.* v. *Helvering* (1935), 296 U. S. 374; *Helvering* v. *Watts* (1935), 296 U. S. 387; *LeTulle* v. *Scofield* (1940), 308 U. S. 415; *Helvering* v. *Alabama Asphaltic Limestone Company* (1942), 315 U. S. 179.

All of these cases arose under the parenthetical clause. In the *Pinellas* case this Court held that the parenthetical clause was intended to bring within the scope of the definition of a reorganization, transactions that fall short of meeting the tests of a true merger or consolidation. In the *LeTulle* case it was held that the transfer of assets for long-term bonds or part cash and part such bonds did not meet the test. And in the *Alabama Asphaltic Limestone Co.* case, this Court pointed out that "the *Pinellas* case introduced the continuity of interest theory to eliminate those transactions which had no real semblance to a merger or consolidation. * * *" (Page 182)

With the decision of this Court in the *Pinellas* case before it, Congress, in section 112(g)(1) of the Revenue

Act of 1934, rewrote the definition of the term, reorganization.

The following is a comparative print of section 112(g)(1) showing the changes in existing law made by the Revenue Bill of 1934 as it passed the House:

> "~~(1)~~ *(g)* DEFINITION OF REORGANIZATION.—As used in this section and ~~sections 113 and 115~~ *section 113*—
>
> "(1) The term 'reorganization' means (A) a merger or consolidation ~~(including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation)~~, or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place or organization, however effected." [H. R. 7835, 73d Cong., 2d Sess. (1934) 85-86]

It will be seen that in the House Bill the parenthetical clause was completely eliminated. In its report accompanying the bill the Committee on Ways and Means said:

> "In the second place, the definition of a reorganization has been restricted so that the definition will conform more closely to the general requirements of corporation law, and will limit reorganizations to (1) statutory mergers and consolidations; (2) transfers to a controlled corporation, 'control' being defined as an 80-percent ownership; and (3) changes in the capital structure or form of organization.
>
> "By these limitations the committee believes that it has removed the danger that taxable sales can be cast

into the form of a reorganization, while at the same time, legitimate reorganizations, required in order to strengthen the financial condition of the corporation, will be permitted. * * *" [H. Rept. 704, 73d Cong., 2d Sess. (1934) 14]

The following is a comparative print of section 112(g)(1) showing the changes in the House Bill as it passed the Senate and as it was enacted:

"(1) The term 'reorganization' means (A) a ~~merger or consolidation, or (B)~~ *statutory merger or consolidation, or (B) the acquisition by one corporation in exchange solely for its voting stock: of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation, or (C)*, a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or ~~(C)~~ *(D)* a recapitalization, or ~~(D)~~ *(E)* a mere change in identity, form, or place or organization, however effected." [H. R. 7835, 73d Cong., 2d Sess. (1934) 68]

It will be seen that in the bill as it passed the Senate and as it was finally enacted, the word "statutory" was inserted before the terms "merger or consolidation" in Clause (A) and a new Clause (B) was added embracing the acquisition by one corporation of stock or of substantially all the properties of another corporation. This new Clause (B) embraced the same types of transactions as were covered in the parenthetical clause of prior acts, but it was provided that such acquisitions must be in exchange *solely* for voting stock. Thus, in continuing in the definition of a reorganization the types of transactions previously covered by the old parenthetical clause, the Senate and ultimately the Congress, in Clause (B), but not in Clause

(A), imposed its own requirement of a "continuity of interest". [See *Helvering* v. *Southwest Consolidated Corp.*, 315 U. S. 194, 198.]

In its report accompanying the bill, the Committee on Finance said:

> "Your committee is in complete agreement with the purposes of the House bill which aim at tax-avoidance schemes in this connection. However, some modifications are recommended in order to bring about a more uniform application of the provisions in all 48 of the States. *Not all of the States have adopted statutes providing for mergers or consolidations; and, moreover, a corporation of one State cannot ordinarily merge with a corporation of another State.* The committee believes that it is desirable to permit reorganizations in such cases, with restrictions designed to prevent tax avoidance. Consequently, the committee recommends the insertion in the House bill of an addition to the definition of the term 'reorganization' as follows:
>
> "(B) the acquisition by one corporation in exchange solely for its voting stock: of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation;
>
> "The committee believes that these transactions, when carried out as prescribed in this amendment, are in themselves sufficiently similar to mergers and consolidations as to be entitled to similar treatment. It will be noted that the proposed amendment requires that (1) the acquiring corporation must obtain at least 80 per cent of the voting stock and at least 80 per cent of the total number of shares of all other classes of stock of the other corporation, instead of only a majority as provided by the present law; and (2) the acquisition, whether of stock or of substantially all the properties, must be in exchange solely for the voting stock of the acquiring corporation." [S. Rept. 558, 73d Cong., 2d Sess. (1934) 16-17] (Italics ours)

The fact that Clause (B) was added because of the absence of merger and consolidation statutes in some states is affirmative evidence of the deliberate intention of Congress to accept as reorganizations those mergers and consolidations that are effected in accordance with the requirements of those states that do have such statutes. (See Paul, *Selected Studies in Federal Taxation* (1938), Second Series, p. 7; Paul, *Studies in Federal Taxation* (1940), Third Series, p. 60.) The definition of a reorganization as thus amended in the Revenue Act of 1934 was carried forward unchanged in the Revenue Acts of 1936 and 1938.

The parenthetical clause is gone from the statute. Its place has been taken by Clause B of the definition. It is evident that Congress was aware of and in agreement with the continuity of interest test evolved by this Court and wrote it into the statute in express terms and in stricter form than this Court had applied it. But it was written into Clause B only. The several clauses are mutually exclusive. *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378, 384. Congress made Clause A more precise by placing "statutory" as a qualification of "merger or consolidation" and it left the remaining clauses unchanged. Manifestly it intended that such continuity of interest as is inherent in all true mergers would suffice. There is, therefore, no justification for the courts to wrench that test out of the setting in which necessity gave it birth and to ingraft it on precise, carefully chosen statutory language in which such necessity does not inhere.[2]

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[2]The Circuit Court of Appeals gave scant consideration to the legislative history of the amended definition. It held that its previous decision in *Commissioner* v. *Gilmore's Estate*, 130 F. (2d) 791, was "completely dispositive" of the issue (R. 42). It also cited *Morgan Manufacturing Co.* v. *Commissioner*, 124 F. (2d) 602 (C. C. A. 4th) and the decision of this Court in *Helvering* v. *Southwest Consolidated Corp.*, 315 U. S. 194. None of these cases involved the precise point presented here.

The statutes of New Jersey provide in all respects for a true corporate merger within the conventional meaning of that term (R. 26-28). The merger here involved was adopted to meet the tests prescribed by the New Jersey courts in *Outwater* v. *Public Service Corporation*, 103 N. J. Eq. 461, 143 Atl. 729, *aff'd*, 146 Atl. 916. The desirability of the merger is fully demonstrated by the opinion of the Federal Power Commission (R. 3-15). It is clear from the *Outwater* case that Congress, in adopting the standards of New Jersey, could be assured, in the words of the Committee on Ways & Means, that it had "removed the danger that taxable sales could be cast in the form of a reorganization" (R. 34).

Moreover, this is clearly the type of case intended by Congress to be embraced within the non-recognition provisions. Prior to the merger, the stockholders of South Jersey had no voice in the management or operation of the properties and yet they were assured in practical perpetuity of a return of 8% in the form of dividends regardless of the earnings of the particular properties. After the merger, these same stockholders still had no voice in the management and yet they were assured of a return of 8% for 100 years in the form of interest, regardless of the earnings of the properties. Under the test laid down in the *Outwater* case, this provided the stockholders of the lessor with "participation in the merged company relatively as they enjoyed that right in the merging companies". (143 Atl. 729) It was in a very real sense, in the words of the regulations, a "readjustment of continuing interests under modified corporate forms" (R. 30).

During and since 1938, other mergers identical with that involved in this case, have been consummated under the merger statutes of New Jersey and the tax liabilities of a large number of participating stockholders are necessarily involved. The instant proceeding was, therefore,

selected as a test case.[3] The question here presented is also necessarily involved in the cases of all mergers under the laws of other states which permit the exchange of stock for long-term bonds of the continuing companies. The question is obviously one of far-reaching importance. If this case is not reviewed there will be further litigation in other circuits. Since this Court developed the continuity of interest doctrine for a specific purpose under earlier statutes, it should now supervise the attempted extension of that doctrine to different and later statutes, even though there is no presently existing conflict of decisions between circuits.

Conclusion

It is respectfully submitted that this petition for a writ of certiorari should be granted.

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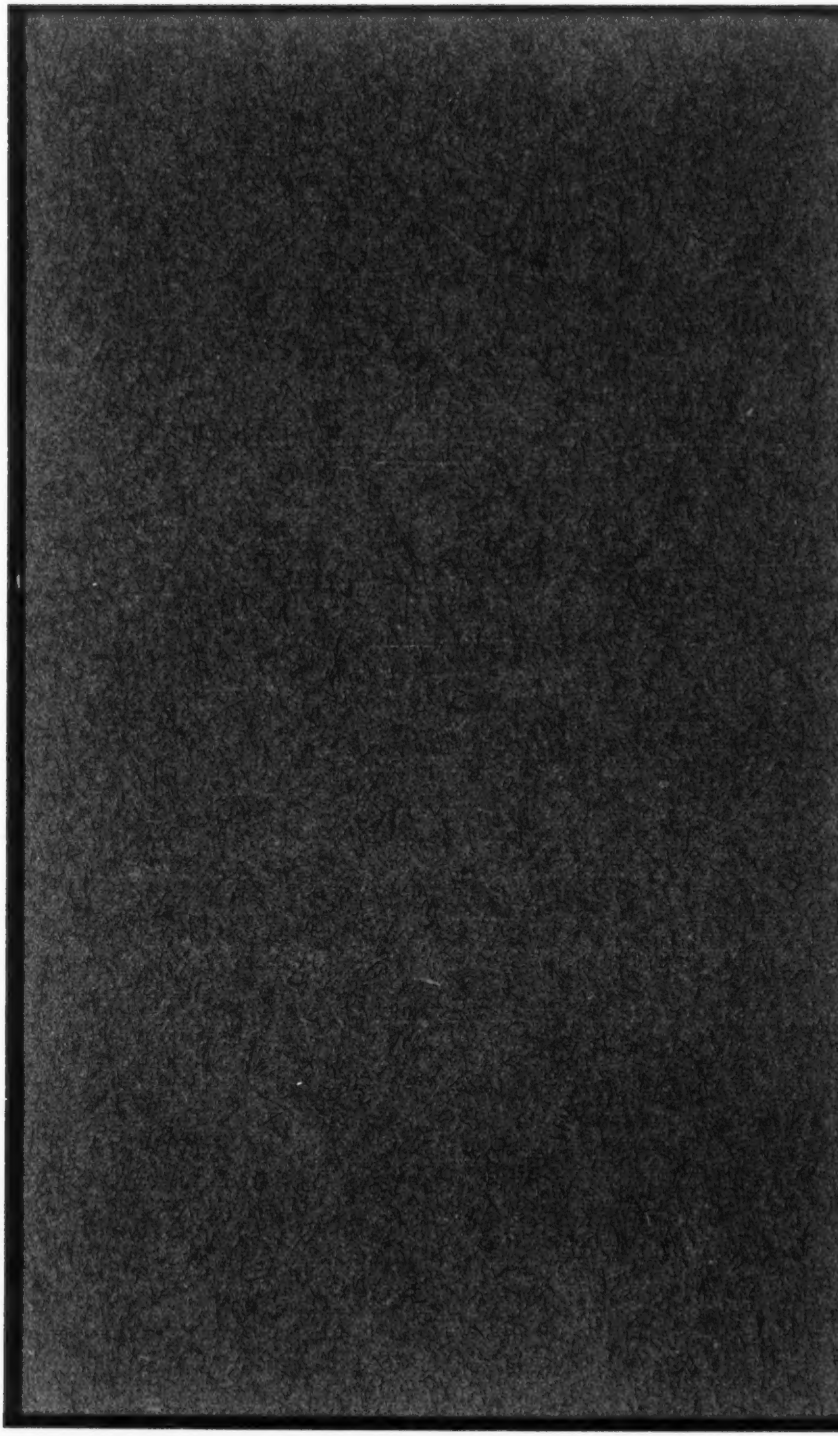
[3]Direct evidence of two other such mergers appear in this Record (R. 3). There is on file in the Circuit Court of Appeals an exhibit, not included in the present Record, which contains direct evidence of two additional mergers. Moreover, we are informed by officials of Public Service Electric & Gas Company that four gas companies were brought in under identical mergers in 1940.

[redacted]



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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 515

FERDINAND W. ROEBLING, III, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 15–25) is not reported. The opinion of the circuit court of appeals (R. 38–46) is reported in 143 F. 2d 810.

JURISDICTION

The judgment of the circuit court of appeals was entered on July 1, 1944 (R. 46–47). The petition for a writ of certiorari was filed on September 28, 1944. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the merger of two corporations under the laws of the State of New Jersey constitutes a reorganization under Section 112 (g) (1) (A) of the Revenue Act of 1938 when the stockholders of one of the merging corporations received in exchange for their stock one hundred year bonds in the reorganized corporation, but no stock.

STATUTE AND REGULATIONS INVOLVED

The relevant provisions of the statute and regulations involved are set forth in the Appendix, *infra*, pp. 11–14.

STATEMENT

The facts in this case were all stipulated and were found, as stipulated, by the Tax Court. The taxpayer was the owner of 166 shares of stock of South Jersey Gas, Electric and Traction Company which had, for tax purposes, a basis to him of $16,600. In June 1903, South Jersey leased all of its franchises, plants, and operating equipment to Public Service Corporation of New Jersey for 900 years. The lessee was to pay rent which, beginning December 1, 1908, amounted to $480,000 per annum. In addition the lessee agreed to pay the interest charges on the lessor's bonded indebtedness, all taxes, insurance, and such sums as were necessary to maintain, repair, improve, and extend the leased properties. All replacements and additions became the property of South Jersey and subject to the terms of the

lease. (R. 16.) South Jersey could enter upon the leased property for the purpose of inspecting it, determining its condition and the character of the management, and whether the covenants of the lease were being complied with. Upon default of the terms of the lease for a period of 30 days, after notice, South Jersey could terminate the lease, reenter and reacquire the property and additions and extensions thereto. In July 1924, this lease was assigned by Public Service Corporation of New Jersey to Public Service Electric and Gas Company which assumed the obligations thereof. (R. 17.) From December 1, 1908, to June 1, 1937, the net rentals received by South Jersey, the lessor company, were distributed to its stockholders at the rate of 8% per annum on the par value of its stock.

South Jersey had 60,000 shares of capital stock of $100 par value outstanding, of which Public Service Electric and Gas Company, the assignee of the lease, held 1,705 shares, and Public Service Corporation of New Jersey, the original lessee, held 15,773 shares. The remaining 42,521 shares were held by other interests. Public Service Corporation of New Jersey held substantially all the voting stock of Public Service Electric and Gas Company. (R. 17.)

On May 10, 1937, the directors of South Jersey and of Public Service Electric and Gas Company adopted a "Plan of Reorganization" under

which it was proposed that the former company be merged in the latter in accordance with the statutes of New Jersey. This plan provided that the stockholders of South Jersey should exchange their stock in South Jersey, dollar for dollar, for eight percent, one hundred year, first mortgage bonds of Public Service Electric and Gas Company. These bonds were to be issued under a prior mortgage of Public Service Electric and Gas Company dated August 1, 1924, and under a supplemental indenture later to be executed. (R. 18–19.) It was expressly provided in the "Agreement of Merger", executed on the same day, that: "The capital stock of the Public Service Electric and Gas Company * * * will not be changed by reason of this agreement." The stock of South Jersey held by Public Service Electric and Gas Company was not to participate in the exchange but was to be delivered up and cancelled. (R. 19–20.) The "Agreement of Merger" was accepted by the stockholders of South Jersey and of Public Service Electric and Gas Company, and approved by the Board of Public Utilities Commissioners of the State of New Jersey and by the Federal Power Commission. With the certificates of the secretaries of the constituent companies as to the confirmatory votes of the stockholders, and the certificates of approval of the Public Utility Commissioners of New Jersey and of the Federal Power Commis-

sion, the "Agreement of Merger" was filed with the Secretary of State of New Jersey on November 17, 1938. (R. 20.)

In accordance with the agreement, the taxpayer received in exchange for his 166 shares of stock in South Jersey, $16,600 principal amount of eight percent bonds which, on November 25, 1938, had a fair market value of $34,777 (R. 21). The Commissioner held that the taxpayer's gain on the exchange of stock for bonds was taxable, and he asserted a deficiency for the calendar year 1938 which the Tax Court sustained, so far as it was based upon this item (R. 21–25). The decision of the Tax Court was affirmed by the circuit court of appeals (R. 38–46).

ARGUMENT

The circuit court of appeals properly determined that the gain realized by the taxpayer in exchanging his stock in South Jersey Gas, Electric and Traction Company for the bonds of Public Service Electric and Gas Company was taxable to him under Section 112 (a) of the Revenue Act of 1938, and that the exchange was not tax free under Section 112 (b) (3), as being effectuated in pursuance of a plan of reorganization, as defined in Section 112 (g) (1) (A). (See Appendix, *infra*, pp. 11–12.) In arriving at this conclusion, the court below followed the decisions of this Court which hold that Congress did not intend the reorganization pro-

visions of the various Revenue Acts to be invoked for postponing what might otherwise be a taxable event unless ownership interests are continued in the reorganized corporation. The circuit court of appeals likewise found that the requisite continuity of ownership was not present in this case.

The requirement of continued ownership is firmly established. *Pinellas Ice Co.* v. *Commissioner*, 287 U. S. 462; *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378; *Nelson Co.* v. *Helvering*, 296 U. S. 374; *Helvering* v. *Watts*, 296 U. S. 387; *LeTulle* v. *Scofield*, 308 U. S. 415; *Helvering* v. *Alabama Asphaltic Limestone Co.*, 315 U. S. 179. The taxpayer contends, however, that the change in Section 112 (g) (1) by the Revenue Act of 1934, c. 277, 48 Stat. 680, indicates a Congressional purpose to make the reorganization provisions applicable when there is, without more, a merger or consolidation under the laws of a particular state (Pet. 7–13).

The changes made in Section 112 (g) (1) by the Revenue Act of 1934, which are set forth in the taxpayer's petition (pp. 9–10), give no support to the construction urged by the taxpayer. Indeed, these changes were prompted by the Congressional desire to prevent tax avoidance and achieve uniformity, and the House Committee report, after stating that the "definition of a reorganization has been restricted", reveals its

familiarity with and approval of the rulings of this Court, holding the reorganization provisions applicable only where corporations undergo mere changes in form "with the stockholders continuing their former interest in the original enterprise."[1] The purpose of the insertion of Section 112 (g) (1) (B) (Appendix, *infra*, p. 12), by the Senate Committee,[2] was to exempt reorganizations which met the requirements there enumerated, and so, by allowing such exemptions even in jurisdictions without statutory provision for mergers and consolidations, to approximate uniformity of treatment. Although the standard there imposed is stricter than that previously applied,[3] there is a complete absence of any indication of an intention to abandon the previously existing requirement of continuity of ownership interests with respect to statutory mergers or consolidations. Plainly, the scheme of uniformity and the abatement of tax avoidance sought by the Senate Committee would not have been achieved by such a device. Taxability would turn on state statutory descriptions of "mergers and consolidations" which vary in their imposition of continuity of interest requirements.

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[1] H. Rep. No. 704, 73d Cong., 2d Sess., pp. 12–15 (1939–1 Cum. Bull. (Part 2) 554, 563–565).

[2] S. Rep. No. 558, 73d Cong., 2d Sess., pp. 16–17 (1939–1 Cum. Bull. (Part 2), 586, 598–599).

[3] *Helvering* v. *Southwest Corp.*, 315 U. S. 194.

Finally, the explanations made regarding the conference bill, in which the Senate amendment was adopted, fail to disclose the Congressional purpose which taxpayer asserts existed.[4] It is indeed strange, if Congress did intend to abrogate the continuity of interest test for statutory mergers and consolidations, that the congressional committees, in their detailed reports on the section, made no mention whatever of this purpose to change the law.

Treasury Regulations 86, Art. 112 (g)-1-3, promulgated under the Revenue Act of 1934, construed the statute as continuing the requirement that continuity of ownership exist in connection with a merger or consolidation under state law. That interpretation has been embodied in all succeeding Treasury Regulations promulgated under subsequent Revenue Acts and under the Internal Revenue Code. Section 112 (g) of the Revenue Act of 1934 was reenacted without change in the Revenue Acts of 1936, c. 690, 49 Stat. 1648, and 1938 (Appendix, *infra,* p. 12), and in the Internal Revenue Code; it was amended, but only as to unrelated matters, by the Revenue Acts of 1939, c. 247, 53 Stat. 862, Sec. 213 (b), and 1943, Pub. Law 235, 78th Cong., 2d Sess. (Feb. 25, 1944), Sec. 121 (d). The fact that Congress, although it had ample opportunity to do so, has not indicated any disagreement with this interpreta-

[4] H. Rep. No. 1385, 73d Cong., 2d Sess., pp. 21-22 (1939-1 Cum. Bull. (Part 2), 627, 632).

tion of the Treasury Department, is persuasive that the construction sought by taxpayer is erroneous. *Douglas* v. *Commissioner,* 322 U. S. 275, 281–282.

The court below relied on *Commissioner* v. *Gilmore's Estate,* 130 F. 2d 791, 794 (C. C. A. 3d), and *Morgan Mfg. Co.* v. *Commissioner,* 124 F. 2d 602 (C. C. A. 4th), in support of its decision. Taxpayer states that those cases do not involve "the precise point presented here." (Pet. 12.) We do not agree. Although there are factual differences between the present case and each of those cases, they do recognize that the continuity of interest test was not removed from application to corporate mergers and consolidations carried out under state law. The *Morgan* case involved Section 112 (g) (1) (A) of the Revenue Act of 1936 and the *Gilmore* case involved the same section of the 1934 Act.

The argument is also made that the requisite continuity of interest was present in this case (Pet. 2, 13). We do not believe that it requires any elaborate analysis to show that when the stockholders of one corporation give up their proprietary interests and assume, in exchange, the position of creditors holding one hundred year, first mortgage bonds of the merged corporation, there is no continuity of ownership. *LeTulle* v. *Scofield,* 308 U. S. 415.

CONCLUSION

The decision of the circuit court of appeals is correct. There is no conflict of decisions. Accordingly, this petition for a writ of certiorari should be denied.

Respectfully submitted,

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OCTOBER, 1944.

APPENDIX

Revenue Act of 1938, c. 289, 52 Stat. 447:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges Solely in Kind.*—

* * * * *

(3) *Stock for Stock on Reorganization.*—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

* * * * *

(g) *Definition of Reorganization.*—As used in this section and section 113—

(1) The term "reorganization" means (A) a statutory merger or consolidation, or (B) the acquisition by one corporation in exchange solely for all or a part of its voting stock: of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation, or (C) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred, or (D) a recapitalization, or (E) a mere change in identity, form, or place of organization, however effected.

* * * * *

Treasury Regulations 101, promulgated under the Revenue Act of 1938:

Art. 112 (g)-1. *Purpose and scope of exception of reorganization exchanges.—Purpose*: Under the general rule, upon the exchange of property, gain or loss must be accounted for if the new property differs in a material particular, either in kind or in extent, from the old property. The purpose of the reorganization provisions of the Act is to except from the general rule certain specifically described exchanges incident to such readjustments of corporate structures, made in one of the particular ways specified in the Act, as are required by business exigencies, and which effect only a readjustment of continuing interests in property under modified corporate forms. Requisite to a reorganization under the Act are a con-

tinuity of the business enterprise under the modified corporate form, and a continuity of interest therein on the part of those persons who were the owners of the enterprise prior to the reorganization. * * * The Act recognizes as a reorganization the amalgamation (occurring in a specified way) of two corporate enterprises under a single corporate structure if there exists among the holders of the stock and securities of either of the old corporations the requisite continuity of interest in the new corporation, but there is not a reorganization if the holders of the stock and securities of the old corporation are merely the holders of short-term notes in the new corporation. In order to exclude transactions not intended to be included, the specifications of the reorganization provisions of the law are precise. Both the terms of the specifications and their underlying assumptions and purposes must be satisfied in order to entitle the taxpayer to the benefit of the exception from the general rule. * * *

Art. 112 (g)-2. *Definition of terms.*— The application of the term "reorganization" is to be strictly limited to the specific transaction set forth in section 112 (g) (1). The term does not embrace the mere purchase by one corporation of the properties of another corporation, for it imports a continuity of interest on the part of the transferor or its stockholders in the properties transferred. If the properties are transferred for cash and deferred payment obligations of the transferee evidenced by short-term notes, the transaction is a sale and not an exchange.

The words "statutory merger or consolidation" refer to a merger or a consolidation effected in pursuance of the corporation laws

of the United States or a State or Territory or the District of Columbia. * * *

Art. 112 (g)–3. *Exchanges solely of stock or securities, or property, solely for stock or securities, in pursuance of plan of reorganization.*—No taxable income is received, nor is a deductible loss sustained, if the shareholders in a corporation a party to the following reorganization transactions exchange stock or securities solely for stock or securities of the same corporation, or of another corporation mentioned, or if one of such corporations transfers property to another of the corporations solely for stock or securities of such other corporation, in pursuance of the plan of reorganization:

(1) The merger of Corporation A, in accordance with statutory authority, into Corporation B; * * *.

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